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Investor's Business Daily

High Corn Prices Drive Up Eggs and Help Cal-Maine Have Fun

Tuesday July 10, 7:00 pm ET

Marilyn Alva

Never mind whether it's the chicken or the egg that comes first.

In the egg business these days, the question is about the ties between ethanol and feed stock.

The relationship is turning out to be a good one for U.S. egg producers, who are clucking all the way to the bank.

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into higher egg prices.

Since feed stock costs are so high, egg farmers have cut back on production.

Egg Supply

With 280 million egg-laying hens left, there are enough eggs for everybody.

But the national flock size of egg-laying hens is now six million less than this time last year, says Gene Gregory, president of United Egg Producers.

"We're having fun in the egg business right now," said Fred Adams, chief executive of Cal-Maine Foods (NasdaqGM:CALM - News), the largest of them all.

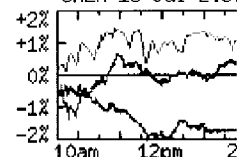
Corn is the common factor. It's a key ingredient in both ethanol and feed stock. Surging demand for the fuel since last fall has caused corn prices to soar about 60%.

That in turn has driven up the cost of feed stock. Why is that a good thing for egg farmers?

The business is all about supply and demand. Reduced supply without a comparable drop in demand translates

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Per-capita consumption has remained steady since 2000 at around 250 to 255 eggs a year, or about five eggs per person per week.

As the largest supplier of fresh shell eggs in the U.S., Cal-Maine has a 16% share of the shell egg market.

It also is the only U.S. egg company out of 250 that is publicly traded.

Cal-Maine sells eggs in 28 states, mainly in the Sun Belt and lower Midwest and mid-Atlantic.

Customers include top supermarket chains and food service distributors, such as Wal-Mart (NYSE:WMT - News), H.E. Butt Grocery, Kroger (NYSE:KR - News), Safeway, Sysco (NYSE:SY - News) and U.S. Foodservice.

Cal-Maine has cut back its own egg supply 1% to 2%. That's more than one might think.

"One or two percent on the supply side affects prices 20% or 30%," Adams said.

"Feed costs are up 10 cents a dozen and egg prices are up 20 cents a dozen. So that leaves us with a good, profitable story," he said.

Cal-Maine's earnings have come back strong in the last two quarters, with the last up 118% over the earlier year to 74 cents a share. Sales in the quarter were up 35% to \$175.2million.

That's a stark turnaround from the prior two years.

In 2006, egg supply was abundant, resulting in lower egg prices. Cal-Maine lost \$1 million, or 4 cents a share. Egg economics were even worse in 2005 when Cal-Maine lost \$10.4 million, or 43 cents a share.

Like oil and corn, eggs are a commodity.

Over the past few years, steady demand for eggs coupled with relatively low feedstock costs kept production levels up and prices low.

So profits were down. "Like any commodity business, it's very cyclical," said Don Dalton, president of the U.S. Poultry & Egg Association. "When you get too many eggs out, their business becomes very unprofitable. Oversupply makes the market go down. Right now, we don't have oversupply."

The U.S. Department of Agriculture forecasts egg price increases of 21% this year on average and continued price strength next year.

How long will the good times last?

As long as ethanol demand remains strong, feed prices are expected to stay high.

"All forecasters that have watched this ethanol issue believe we are going to have high feed costs (for some time)," Gregory said.

The U.S. produced nearly 5 billion gallons of ethanol last year. The USDA forecasts it will top 10 billion gallons by 2009 and 12 billion gallons by 2015.

Egg industry experts are concerned that subsidized ethanol production could drive egg prices to dangerous levels, however. High prices might inspire producers to step up production.

"Oversupply would be devastating," Dalton said. That doesn't seem a problem, at least in the

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near term.

Cal-Maine keeps an eye on costs. "Over the years, they've learned to be very cost efficient," Dalton said. "That's probably their chief attribute. And they are a good marketer of eggs."

Costs might rise some as the firm changes the way it treats its flock of hens to meet treatment guidelines set by animal rights groups, the company warned. For example, it's increasing cage space and modifying forced molting practices. However, costs related to these changes so far have been passed on to customers.

Though egg consumption has come back from a low of 234 per-capita in 1991, when eggs got a bad rap due to cholesterol concerns, their numbers have since grown on more positive health news.

Acquisitions

Growth follows population growth, about 1% a year.

Since demand is growing only 1% a year, Cal-Maine grows mainly by acquiring other egg producers. That way it's not increasing overall supply -- just its share of it.

Cal-Maine has bought about a dozen companies since the late 1980s. In January, it bought the remaining 50% interest in Green Forest Foods. It gained control of Hillandale LLC in 2005.

The firm recently agreed to buy the Arkansas-based shell-egg business of poultry producer George's, with minority partner Country Creek Farms.

Cal-Maine intends to keep buying other firms.

It also is growing revenue from its higher-margin specialty shell eggs. Those include organic, cage free and reduced-cholesterol eggs. It does so through its trademarked Farmhouse brand and exclusive license agreements with Eggland's Best.

In 2006, specialty eggs made up about 14% of total egg sales.

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